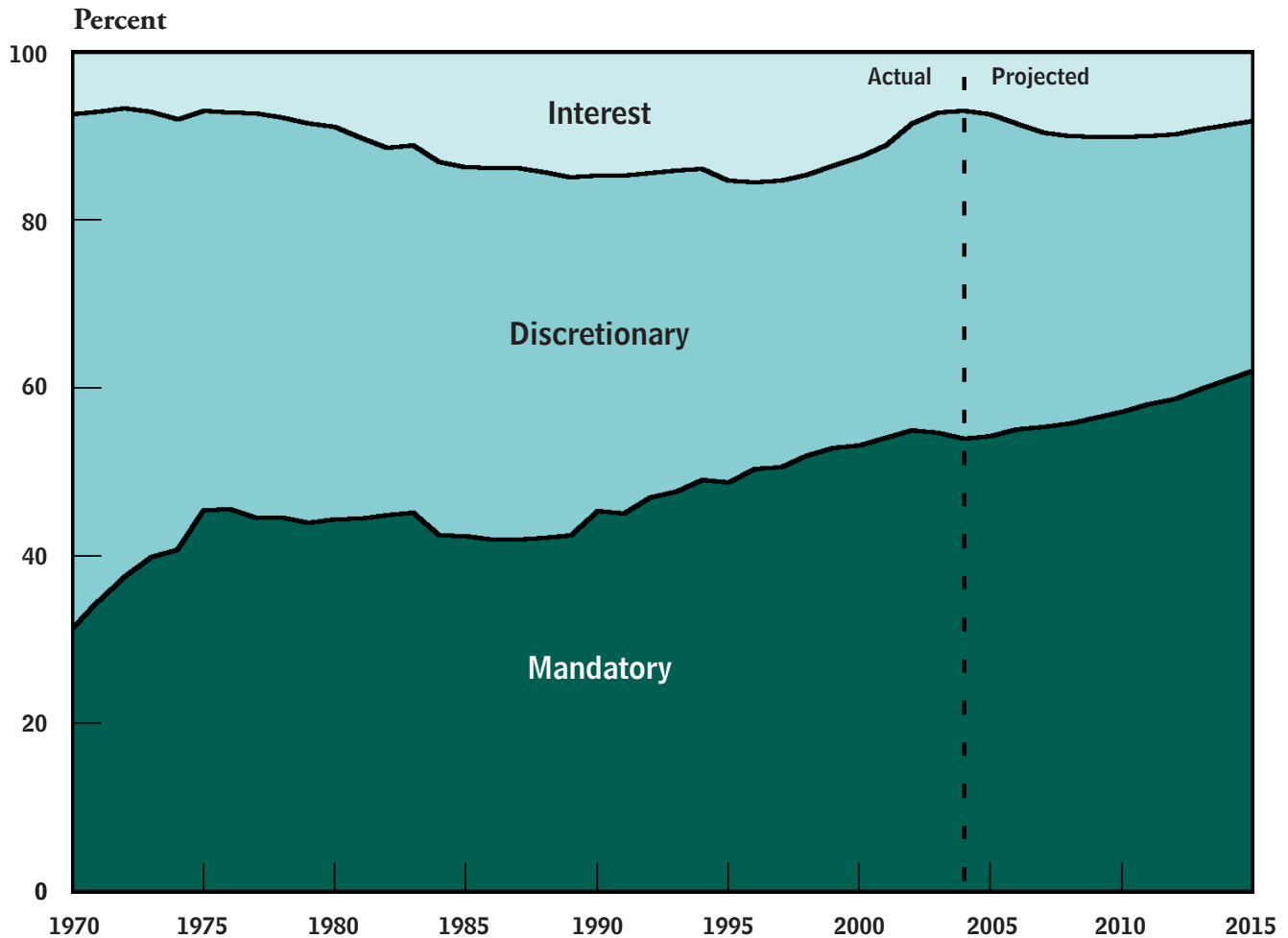
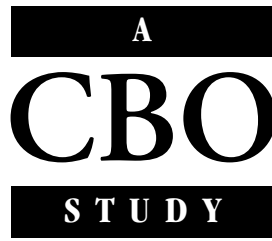


The Budget and Economic Outlook: Fiscal Years 2006 to 2015

Type of Spending as a Share of Total Outlays



JANUARY 2005



The Budget and Economic Outlook: Fiscal Years 2006 to 2015

January 2005

Notes

Unless otherwise indicated, all years referred to in describing the economic outlook are calendar years; otherwise, the years are federal fiscal years (which run from October 1 to September 30).

Numbers in the text and tables may not add up to totals because of rounding.

Some of the figures in Chapter 2 and Appendix D use shaded vertical bars to indicate periods of recession. A recession extends from the peak of a business cycle to its trough.

Data for real (inflation-adjusted) gross domestic product are based on chained 2000 dollars.



Preface

This volume is one of a series of reports on the state of the budget and the economy that the Congressional Budget Office (CBO) issues each year. It satisfies the requirement of section 202(e) of the Congressional Budget Act of 1974 for CBO to submit to the Committees on the Budget periodic reports about fiscal policy and to provide baseline projections of the federal budget. In accordance with CBO's mandate to provide impartial analysis, the report makes no recommendations.

The baseline spending projections were prepared by the staff of CBO's Budget Analysis Division under the supervision of Robert Sunshine, Peter Fontaine, Janet Airis, Thomas Bradley, Kim Cawley, Paul Cullinan, Jeffrey Holland, and Jo Ann Vines. The revenue estimates were prepared by the staff of the Tax Analysis Division under the supervision of Thomas Woodward, Mark Booth, and David Weiner, with assistance from the Joint Committee on Taxation. (A detailed list of contributors to the spending and revenue projections appears in Appendix G.)

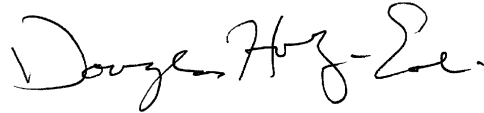
The economic outlook presented in Chapter 2 was prepared by the Macroeconomic Analysis Division under the direction of Robert Dennis. John F. Peterson, Robert Arnold, and Christopher Williams carried out the economic forecast and projections. David Brauer, Ufuk Demiroglu, Tracy Foertsch, Eva de Francisco, Douglas Hamilton, Juann Hung, Kim Kowalewski, Mark Lasky, Angelo Mascaro, Shinichi Nishiyama, Benjamin Page, Frank Russek, Robert Shackleton, and Sven Sinclair contributed to the analysis. Adam Gordon, Brian Mathis, and Amrita Palriwala provided research assistance.

CBO's Panel of Economic Advisers commented on an early version of the economic forecast underlying this report. Members of the panel are Andrew B. Abel, Alan Blinder, Dan Crippen, William C. Dudley, Martin Feldstein, Robert J. Gordon, Robert E. Hall, Robert Glenn Hubbard, Lawrence Katz, Catherine L. Mann, Allan H. Meltzer, Laurence H. Meyer, William D. Nordhaus, June E. O'Neill, Rudolph G. Penner, James Poterba, Robert Reischauer, and Alice Rivlin. Martin Baily, Nada Eissa, Paul Fronstin, and Casey Mulligan attended the panel's meeting as guests. Although CBO's outside advisers provided considerable assistance, they are not responsible for the contents of this report.

Jeffrey Holland wrote the summary. Barry Blom, Mark Booth, Ann Futrell, and Eric Schatten wrote Chapter 1 (David Newman wrote Box 1-1). Robert Arnold was the lead author for Chapter 2. Gerard Trimarco and Christina Hawley Sadoti authored Chapter 3, with assistance from Thomas Bradley and Eric Schatten. Mark Booth and Thomas Woodward were the lead authors for Chapter 4. Ellen Hays wrote Appendixes A and C; Frank Russek and Barry Blom, Appendix B; and David Brauer, Appendix D. Robert Arnold prepared Appendix E, and Ann Futrell compiled Appendix F. Jennifer Smith produced the glossary.

Christine Bogusz, Janey Cohen, Loretta Lettner, Leah Mazade, John Skeen, and Christian Spoor edited the report. Marion Curry, Linda Lewis Harris, and Denise Jordan-Williams

assisted in its preparation. Maureen Costantino designed the cover and prepared the report for publication. Lenny Skutnik and Carter Campbell printed the initial copies, and Annette Kalicki and Simone Thomas, with assistance from Martina Wojak-Piotrow, produced the electronic versions for CBO's Web site (www.cbo.gov).

A handwritten signature in black ink, reading "Douglas Holtz-Eakin". The signature is fluid and cursive, with the first name "Douglas" being the most prominent.

Douglas Holtz-Eakin
Director

January 2005

Summary *xiii*

1

The Budget Outlook *1*

A Review of 2004 *5*

The Concept Behind CBO's Baseline Projections *5*

Uncertainty and Budget Projections *6*

The Long-Term Outlook *10*

Changes to the Budget Outlook Since September 2004 *11*

The Outlook for Federal Debt *18*

Trust Funds and the Budget *22*

2

The Economic Outlook *25*

Overview of CBO's Two-Year Forecast *25*

The Importance of Productivity Growth for Economic and
Budget Projections *26*

The Outlook for 2005 and 2006 *28*

The Economic Outlook Through 2015 *41*

Taxable Income *46*

Changes in CBO's Outlook Since September 2004 *47*

A Comparison of Forecasts *49*

3

The Spending Outlook *51*

Mandatory Spending *53*

Discretionary Spending *64*

Net Interest *70*

4

The Revenue Outlook *75*

Revenues by Source *76*

Revenue Projections in Detail *77*

Uncertainty in the Revenue Baseline *94*

Revisions to CBO's September 2004 Revenue Projections *95*

The Effects of Expiring Tax Provisions *96*

A	How Changes in Economic Assumptions Can Affect Budget Projections 103
	Higher Real Growth 103
	Higher Interest Rates 105
	Higher Inflation 105
	Wages and Salaries as a Higher Percentage of GDP 106
B	The Treatment of Federal Receipts and Expenditures in the National Income and Product Accounts 107
	Conceptual Differences Between the NIPAs' Federal Sector and the Federal Budget 107
	Differences in Accounting for Major Transactions 108
	Presentation of the Federal Government's Receipts and Expenditures in the NIPAs 114
C	Budget Resolution Targets and Actual Outcomes 117
	Elements of the Analysis 117
	Comparing the Budget Resolution and Actual Outcomes for Fiscal Year 2004 118
	Comparing Budget Resolutions and Actual Outcomes for Fiscal Years 1980 Through 2004 120
	Differences as a Percentage of Actual Revenues or Outlays 123
D	Forecasting Employers' Contributions to Defined-Benefit Pensions and Health Insurance 125
	Contributions to Defined-Benefit Pensions 125
	Contributions to Medical Insurance Premiums 126
	Implications for Projecting Income Shares and Revenues 127
E	CBO's Economic Projections for 2005 to 2015 129

F**Historical Budget Data** *133***G****Contributors to the Revenue and Spending Projections** *147*Revenue Projections *147*Spending Projections *147***Glossary** *151*

Tables

S-1.	CBO's Baseline Budget Outlook	xiv
S-2.	Changes Since September 2004 in CBO's Estimate of the Cumulative Deficit for 2005 to 2014	xv
S-3.	CBO's Economic Projections for Calendar Years 2005 to 2015	xviii
1-1.	Comparison of CBO's January 2005 and September 2004 Baseline Deficits or Surpluses	2
1-2.	CBO's Baseline Budget Projections	3
1-3.	The Budgetary Effects of Selected Policy Alternatives Not Included in CBO's Baseline	8
1-4.	Changes in CBO's Baseline Projections of the Deficit Since September 2004	14
1-5.	CBO's Baseline Projections of Federal Debt	20
1-6.	CBO's Baseline Projections of Trust Fund Surpluses	22
2-1.	CBO's Economic Projections for Calendar Years 2004 to 2015	26
2-2.	Key Assumptions in CBO's Projection of Potential Output	45
2-3.	CBO's Current and Previous Economic Projections for Calendar Years 2004 to 2014	48
2-4.	Comparison of CBO, <i>Blue Chip</i> , and Administration Forecasts for 2004 to 2010	50
3-1.	CBO's Projections of Spending Under Baseline Assumptions	52
3-2.	Average Annual Rates of Growth in Outlays Under CBO's Baseline	53
3-3.	CBO's Baseline Projections of Mandatory Spending	56
3-4.	CBO's Baseline Projections of Offsetting Receipts	61
3-5.	Sources of Growth in Mandatory Spending	63
3-6.	Costs for Mandatory Programs That CBO's Baseline Assumes Will Continue Beyond Their Current Expiration Dates	66
3-7.	Defense and Nondefense Discretionary Outlays, 1985 to 2005	69
3-8.	Growth in Discretionary Budget Authority, 2004 to 2005	70
3-9.	CBO's Baseline Projections of Discretionary Spending for Homeland Security	71
3-10.	CBO's Projections of Discretionary Spending Under Alternative Paths	72
3-11.	CBO's Baseline Projections of Federal Interest Outlays	74

Tables (Continued)

4-1.	CBO's Projections of Revenues	78
4-2.	CBO's Projections of Individual Income Tax Receipts and the NIPA Tax Base	79
4-3.	Actual and Projected Capital Gains Realizations and Taxes	84
4-4.	CBO's Projections of Social Insurance Tax Receipts and the Social Insurance Tax Base	85
4-5.	CBO's Projections of Social Insurance Tax Receipts, by Source	88
4-6.	CBO's Projections of Corporate Income Tax Receipts and Tax Bases	89
4-7.	CBO's Projections of Excise Tax Receipts, by Category	92
4-8.	CBO's Projections of Other Sources of Revenue	94
4-9.	Changes in CBO's Projections of Revenues Since September 2004	96
4-10.	Effect of Extending Tax Provisions That Will Expire Before 2015	99
A-1.	Estimated Effects of Selected Economic Changes on CBO's Baseline Budget Projections	104
B-1.	Relationship of the Budget to the Federal Sector of the National Income and Product Accounts	110
B-2.	Projections of Baseline Receipts and Expenditures as Measured by the National Income and Product Accounts	115
C-1.	Comparison of Budget Resolution Targets and Actual Budget Totals, 2004	118
C-2.	Sources of Differences Between Budget Resolution Targets and Actual Budget Totals, 2004	119
C-3.	Sources of Differences Between Budget Resolution Targets and Actual Budget Totals, 1980 to 2004	121
E-1.	CBO's Year-by-Year Forecast and Projections for Calendar Years 2005 to 2015	130
E-2.	CBO's Year-by-Year Forecast and Projections for Fiscal Years 2005 to 2015	131
F-1.	Revenues, Outlays, Deficits, Surpluses, and Debt Held by the Public, 1962 to 2004 (Billions of dollars)	134
F-2.	Revenues, Outlays, Deficits, Surpluses, and Debt Held by the Public, 1962 to 2004 (Percentage of GDP)	135
F-3.	Revenues by Major Source, 1962 to 2004 (Billions of dollars)	136

Tables (Continued)

F-4.	Revenues by Major Source, 1962 to 2004 (Percentage of GDP)	137
F-5.	Outlays for Major Spending Categories, 1962 to 2004 (Billions of dollars)	138
F-6.	Outlays for Major Spending Categories, 1962 to 2004 (Percentage of GDP)	139
F-7.	Discretionary Outlays, 1962 to 2004 (Billions of dollars)	140
F-8.	Discretionary Outlays, 1962 to 2004 (Percentage of GDP)	141
F-9.	Outlays for Mandatory Spending, 1962 to 2004 (Billions of dollars)	142
F-10.	Outlays for Mandatory Spending, 1962 to 2004 (Percentage of GDP)	143
F-11.	Deficits, Surpluses, Debt, and Related Series, 1962 to 2004	144
F-12.	Standardized-Budget Deficit or Surplus and Related Series, 1962 to 2004 (Billions of dollars)	145
F-13.	Standardized-Budget Deficit or Surplus and Related Series, 1962 to 2004 (Percentage of potential GDP)	146

Figures

S-1.	Total Revenues and Outlays as a Percentage of GDP, 1962 to 2015	xvi
S-2.	Type of Spending as a Share of Total Outlays, 1970 to 2015	xvii
1-1.	The Total Deficit or Surplus as a Percentage of GDP, 1967 to 2015	1
1-2.	Debt Held by the Public as a Percentage of GDP, 1940 to 2015	4
1-3.	Uncertainty of CBO's Projections of the Budget Deficit or Surplus Under Current Policies	11
1-4.	Total Federal Spending for Medicare and Medicaid Under Different Assumptions About Excess Cost Growth	12
1-5.	Debt Subject to Limit, October 2003 to September 2006	21
1-6.	Annual Social Security Trust Fund Surpluses, Excluding Interest	23
2-1.	Total Factor Productivity	27
2-2.	Business Fixed Investment	30
2-3.	Corporate Retained Earnings	32
2-4.	Real Personal Consumption Expenditures	33
2-5.	Payroll Employment and Real Labor Compensation	34

Figures (Continued)

2-6.	Real Trade-Weighted Value of the U.S. Dollar	36
2-7.	Index of Monetary and Financial Conditions	38
2-8.	Interest Rates	39
2-9.	The Consumer Price Index: Total and Core Measures	40
2-10.	The Consumer Price Index: Shelter and Core Measures	41
2-11.	Total Share of GDP for Income Categories That Affect Revenue Projections	46
2-12.	Labor Income and Wages and Salaries	47
3-1.	Major Components of Spending, 1962 to 2004	55
3-2.	Discretionary Funding and Outlays, 1985 to 2005	64
3-3.	Nondefense Discretionary Funding, by Budget Function, 2005	68
4-1.	Total Revenues as a Share of GDP, 1946 to 2015	75
4-2.	Annual Growth of Federal Revenues and GDP, 1960 to 2015	76
4-3.	Revenues, by Source, as a Share of GDP, 1960 to 2015	77
4-4.	Capital Gains Realizations as a Share of GDP, Calendar Years 1990 to 2015	83
D-1.	Employers' Hourly Health Insurance Costs	127

Boxes

1-1.	Appropriations for the Global War on Terrorism	6
2-1.	Data Revisions and the Productivity Boom of the Late 1990s	29
2-2.	Is the Price of Oil Going to Fall?	42
3-1.	Categories of Federal Spending	54
4-1.	Tax Bases and Tax Liability	80
4-2.	The Growing Significance of the Alternative Minimum Tax in CBO's Projections	86
4-3.	Special Factors in the Projections for Corporate Profits and Receipts	90

